Lesson 3: Insufficient financial runway

By Allon Raiz

4 Nov 2020

In this ongoing series of articles, Allon Raiz shares some of the most important lessons he has learned using a sequence that mirrors the typical stages of any entrepreneurial journey - from ideation through to scaling a business.

Source: pixabay.com

There are two funding rules of thumb that too few startup entrepreneurs are aware of. The first is that the timeframe you have predicted to break even will normally be double that time in reality.

The second is that the funding you need, according to your predictions, will turn out to be four times more than what you thought. These rules of two and four have massive implications for any business's ability to survive the initial months and years of its existence.

As entrepreneurs, we fall in love with our ideas and tend to overestimate the market acceptance of those ideas. As such, our beautiful Excel spreadsheets reflect a linear if not exponential growth in sales. This is generally exacerbated by our predicted expenses being completely inaccurate and understated with numerous missing line items.

#20Lessons20Years: Lesson 1: Am I really an entrepreneur?
Allon Raiz 10 Mar 2020

The two most common forms of startup funding for small businesses are personal savings and credit card facilities. This is followed by the three Fs – friends, fools and family – to whom we present a magnificent j-curve of our three-year forecast while trying to convince them to part with their money.

Our funding requirements show our dear friends, fools and family a clear terminal point after which plenty of monies will be flowing in to pay back these loans. Because it's embarrassing to approach family and friends for funding, we feel compelled to present the lowest possible amount we need to borrow with the quickest possible payback period. And so, when our "sure thing" doesn't pan out in the way our Excel spreadsheet said it would, we find it difficult to go back to our "financiers" to either delay repayment or ask for more money. We are then forced to either shut down the business or find an alternative source of funding.

Be creative in your approach to funding

21 Oct 2020

The time and emotional energy we use to manage our current "financiers" and to find new financiers would be better used in selling, iterating our product or ensuring better delivery of the product or service – all of which are bound to be screamingly important and urgent in themselves.

Time taken away from sales, iteration and delivery will decrease the probability of sales which will in turn reduce the possibility of repaying existing loans thus creating even more demand for new financiers and managing current ones. A vicious cycle has begun that few small businesses will live through.

The correct way to finance a business is to overestimate your costs, to significantly underestimate your sales, and to provide additional financial buffers for unknowns. Your mental model needs to be that you will approach the money well (financier) only once. Ideally you should be spending all the necessary time and energy upfront to find a sufficient amount of funding with an incredibly conservative payback period. To use an aviation metaphor, you need power in order to take off and fly. Losing power during take-off will result in a disastrous crash.

#20Lessons20Years: Lesson 2: Is there really a market?

Allon Raiz 13 Mar 2020

The funding element of a business is a component of strategy that continues to be important throughout the lifecycle of the business. In the beginning, it's about having the right type of funding from the right type of funder in the right quantity. This phase must see the startup business through the valley of death – the point of inception through to cash-flow breakeven.

The funding strategy then needs to continue beyond this point to include sufficient cash flow for scaling the business, appropriate funding for acquisitions and diverse sources of funding for expansion into new geographies. Ignore viewing and finessing long-term funding as a crucial element of long-term business strategy at your own peril!

ABOUT ALLON RAIZ

Allon Raiz is the CEO of Raizcorp. In 2008, Raiz was selected as a Young Global Leader by the World Economic Forum, and in 2011 he was appointed for the first time as a member of the Global Agenda Council on Fostering Entrepreneurship. Following a series of entrepreneurship master classes delivered at Oxford University in 2014, 2015 and 2016, Raiz has been recognised as the Entrepreneur-in-Residence at the University of Oxford's Saïd Business School.

- What it takes to go from side hustling to successful entrepreneurship - 7 May 2024

- Learning to pitch better: The value of feedback from investors and financiers - 19 Apr 2023
- Want to grow your business? Get rid of the 'fax machines' - 15 Dec 2021
- #PolishYourPitch: Pitching Tip 9: The simpler, the better - 20 Jul 2021
- #PolishYourPitch: Pitching Tip 8: Be specific - 13 Jul 2021

View my profile and articles...